Management Discussion and Analysis

Industry structure and development

Global economy

World economic growth in 2017 stood at 3.8%, the fastest since 2011. Notably, sustained trade and investment powered the global upturn. More rapid growth in the Eurozone, emerging Asia and the US propelled this acceleration in global output. On the back of supportive global tailwinds, growth is expected to rise to 3.9% in both 2018 and 2019. Concerns, however, remain owing to geopolitical constraints and a shift towards protectionism [Source: International Monetary Fund (IMF)]. Moreover, on the inflation front, while the escalation in commodity prices, especially crude oil, led to an increase in fuel prices and thereby headline-inflation in advanced economies, core-price inflation continued to remain range bound.

Economies in the Euro area are narrowing down excess capacity with the help of favourable monetary policies. In addition, the cyclical upswing and effects of the expansionary fiscal policies adopted by the US are likely to run their course in the medium term. With easy financial conditions and low inflation that has required protracted monetary policy accommodation, a potential build-up of financial vulnerabilities may give way to rapid tightening of global financial conditions, adversely impacting confidence and growth. Other risks comprise a shift towards inward-looking policies that jeopardise international trade and may lead to geopolitical tensions and strife.

In contrast, emerging market and developing economies (EMDEs), through enhanced capacity utilisation for labour and capital, present headroom for growth. According to the IMF, medium-term growth in EMDEs will be close to their 2018 and 2019 levels. This projection follows from the expected increase in India's growth that will offset China's gradual slowdown and emerging Europe's return to its lower-trend growth rate.

Global growth pattern (%)

	2017	2018 (P)	2019 (P)
World output	3.8	3.9	3.9
Advanced economies	2.3	2.5	2.2
United States	2.3	2.9	2.7
Euro area	2.3	2.4	2.0
Japan	1.7	1.2	0.9
Australia	2.3	3.1	3.0
Other advanced economies*	2.7	2.7	2.6
Emerging market and developing economies	4.8	4.9	5.1
Emerging and developing Asia	6.5	6.5	6.6
Sub-Saharan Africa	2.8	3.4	3.7

*Excludes the United States, Canada, the UK, Euro area countries, and Japan | P: Projections
[Source: International Monetary Fund (IMF)]

Indian economy

Despite short-term challenges, the Indian economy continued to be one of the fastest-growing major economies of the world. The year saw the Government introduce the unified tax regime – Goods and Services Tax (GST) – to create a single marketplace. While initially there were some transitory problems faced along the supply chain and compliance responsibilities, India Inc. welcomed the move towards greater transparency and formalisation in the economy. Consumer sentiments remained subdued for the first half of the year, while the second half witnessed a revival in economic activity.

The economy grew by 7.7% in the fourth quarter, demonstrating resilience and depth, having endured the twin impacts of demonetisation and GST. The overall growth rate for the entire fiscal stood at 6.7%. During FY 2017-18, the international rating agency Moody's raised India's investment grade to Baa3, the first upgrade in 14 years; changing the outlook from stable to positive. India also entered the top 100 of the World Bank's 'Ease of Doing Business' index. The Economic Survey 2017-18 forecasts a growth rate of 7-7.5% for FY 2018-19, citing private investments and exports as the two engines of growth.

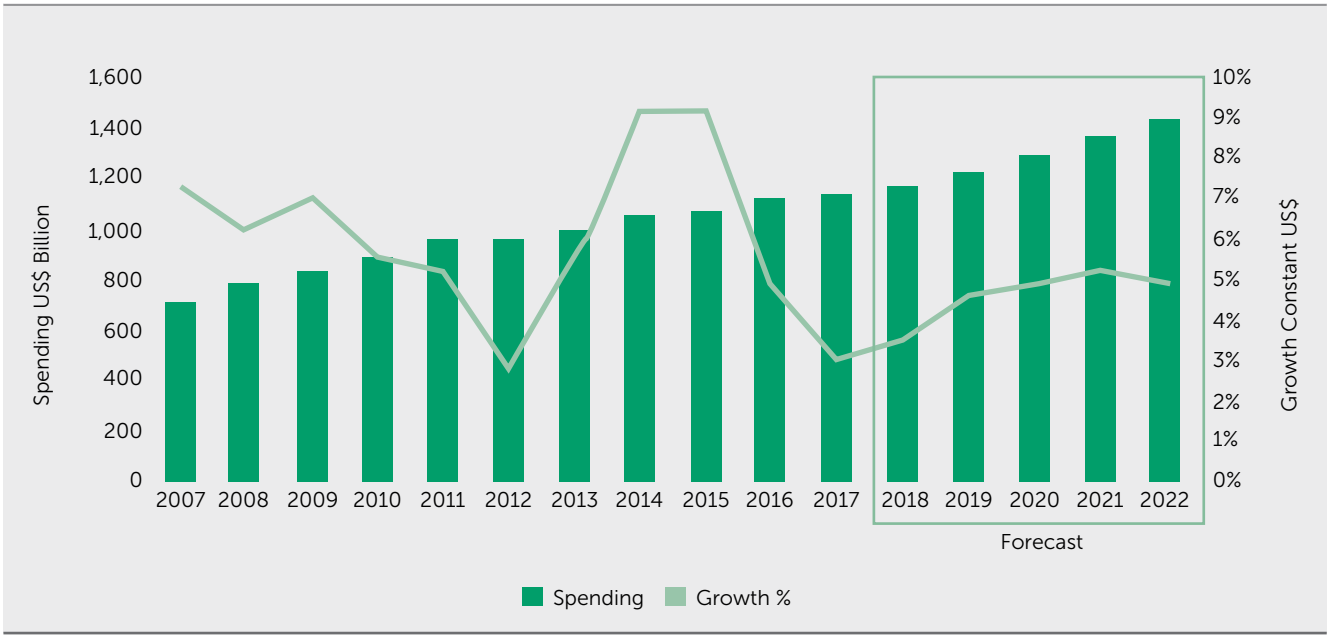
Global pharmaceutical industry

Growing at an average compound annual growth rate (CAGR) of 3 to 6%, the global pharmaceutical spending is projected to reach US$ 1.4 Trillion by 2022, from US$ 1.1 Trillion in 2017. Demographic changes in society, improved purchasing power and overall economic progress will also elevate spending. Globally, governments are implementing pharmaceutical costs controls to improve affordability and access.

A significant proportion of the spending growth in developed markets, will be driven by ageing population, a rise in speciality medicines and innovations in oncology, autoimmune and diabetes treatments. Developed markets are expected to grow at 2-5% CAGR, from US$ 753 Billion in 2017 to reach US$ 915-945 Billion in 2022.

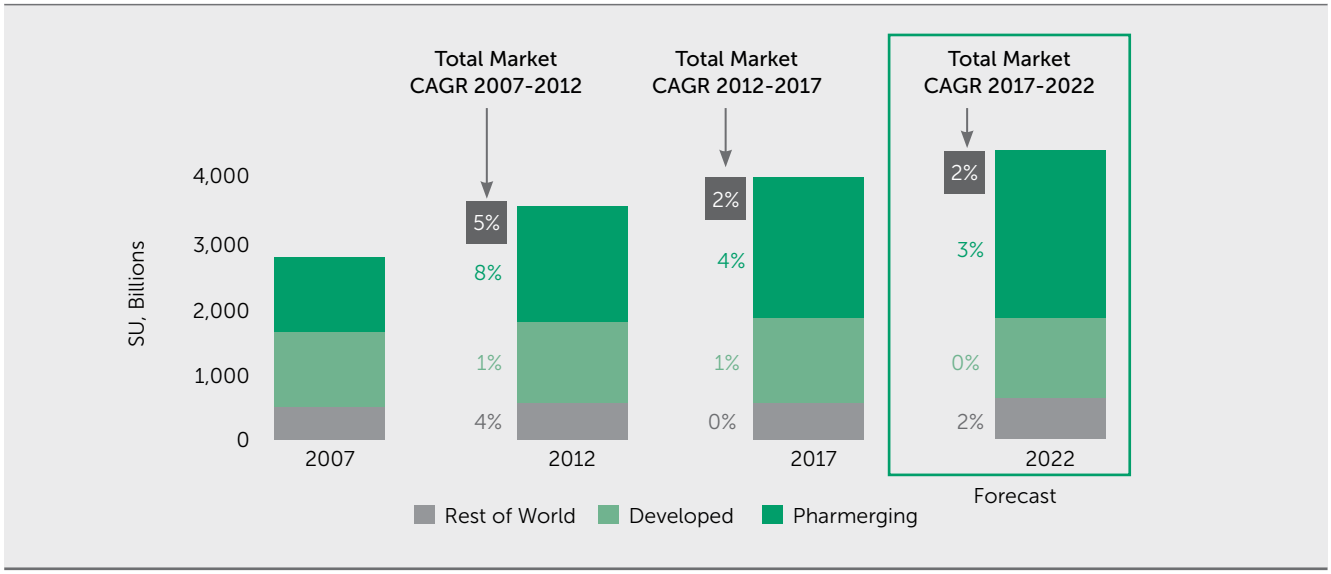
Growing population and disposable incomes, coupled with rising aspirations for better healthcare, will drive spending in pharmerging markets. Majority of medicine use and expenditure in these regions continues to be for non-branded drugs, and payment is primarily out-of-pocket, ultimately linking medicine spending growth to economic growth of economies. Pharmerging markets are projected to grow at 6-9% CAGR, from US$ 270 Billion in 2017 to reach US$ 345-375 Billion in 2022 – the fastest-growing markets in the world. [Source: IQVIA Market Prognosis, October 2017]

Global pharmaceutical market spending and growth 2007-22



[Source: IQVIA Market Prognosis, September 2017; IQVIA Institute October 2017]

Global medicine volume growth 2007-22



Source: IQVIA Institute, October 2017
Notes: CAGR = Compound Annual Growth Rate
Developed: USA, EU5 (Germany, France, Italy, UK and Spain), Japan, Canada, South Korea and Australia
Pharmerging: China, Brazil, Russia, India, Venezuela, Poland, Argentina, Turkey, Mexico, Vietnam, South Africa, Thailand, Indonesia, Romania, Egypt, Pakistan, Ukraine, Algeria, Colombia, Nigeria, Saudi Arabia and Russia

Regional spending

Regions	2017	2013-2017 CAGR	2022	2018-2022
	(US$ Billion)	(%)	(US$ Billion)	(%)
Developed	753	5.8	915-945	2-5
Pharmerging	270	9.7	345-375	6-9
Rest of the World	112	2	125-155	2-5
Global	1,135	6.2	1,415-1,445	3-6

[Source: IQVIA Market Prognosis, September 2017; IQVIA Institute October 2017]

Spending by region and product type in 2022

[Source: IQVIA Market Prognosis, October 2017]

Market for innovators

Speciality medicines overtook traditional medicines for the 10th year in a row. Innovation in speciality medicines and declining growth in conventional medicines drove the speciality share of global spending from 19% in 2007 to 32% in 2017.

Speciality is likely to reach 48% of spending in developed markets by 2022. In these markets, the speciality share will rise more slowly than the last few years, surpassing half of the medical spending in the US, Germany, France, Spain and the UK, in 2022.

Overall, the growth of speciality medicines will be constrained by cost and access controls and a greater focus on assessment of value. [Source: IQVIA Market Prognosis, October 2017]

Generics market

Globally, the market for generics, particularly in the Emerging Markets and Developing Economies (EMDEs) benefited from government initiatives to promote production and use of such drugs. Patent expiry of branded products fuels the growth of generic drugs market.

Affordable generic substitutes will drive improvement in generic penetration globally driving demand and growth. Regional markets that are still nascent represent new opportunities for expansion.

Key pharmaceutical markets

Regulated markets

USA

Being the global market leader, the US is responsible for the bulk of the growth in pharmaceutical spending. The US pharmaceutical market is projected to grow by 4-7% CAGR from US$ 467 Billion in 2017 to US$ 585-615 Billion in 2022. [Source: IQVIA Market Prognosis, October 2017].

The country's key pharmaceuticals regulator, US Food and Drug Administration (FDA) revealed that it approved 46 novel drugs in 2017 – highest in two decades and more than twice the number approved in 2016. Indian pharmaceutical companies in 2017 received final approvals from the USFDA for 304 abbreviated new drug applications (ANDAs) out of the total 846 given globally, accounting for ~36% of the overall approvals. This is up 43% from 211 ANDAs in 2016. In October 2017, the FDA issued a draft guidance, under the revised Generic Drug User Fee Amendments (GDUFA II), describing a new fee structure for generic drug-makers which will further augment its existing resources. The agency is expected to formally issue a framework in 2018 to accelerate the drug approval process even more. This will ensure that patients have access to safe, high-quality, and affordable generic drugs with greater predictability and timeliness for review of generic drug applications. All of this augur well for pharmaceutical players keen on consolidating their presence in the US drug market, mainly generics.

The current administrative climate in the US is conducive to moderated and constant drug prices as there is greater scrutiny of drug pricing policy in the US, with the price of a new drug being weighed against the value it delivers. Patent expiry and the consequent loss of brand exclusivity are expected to lower US drug prices. The US will witness patent expiry of brands worth US$ 77.2 Billion in the next 5 years, providing further growth impetus for generic industry.

EU5

Europe's increasing patient pool for chronic diseases and changing over-the-counter drug scenario are driving its pharmaceutical market. Most pharmaceutical companies are diversifying their product portfolio and evaluating inorganic growth opportunities in the European market. Expanding product reach, particularly in non-US markets, is critical to spreading out the risk base of these pharmaceutical companies. The recent spurt in mergers and acquisitions (M&As) in the region is an indicator of Europe's evolution into a key opportunity market for most players in the sector.

Growth in medicine spending in the top five European (Germany, France, Italy, Spain and the UK) markets will increase from US$ 154 Billion in 2017 to US$ 170-200 Billion in 2022, growing at an estimated 1-4% CAGR [Source: IQVIA Market Prognosis, October 2017]. These five markets cumulatively will account for 69% of the European pharmaceutical market in 2022 [Source: Evaluate European Pharma Outlook report]. The European Medicines Agency (EMA) will shift from the UK to the Netherlands, as a direct consequence of Brexit. This may affect the drug approval process; and thereby the revenue streams of pharmaceutical companies.

Japan

Japan's pharmaceutical spending stood at around US$ 85 Billion in 2017. It is estimated to continue to grow at a sluggish pace to reach US$ 85-89 Billion by 2022. The country's high dependency ratio and complex regulatory procedures inhibit growth in the sector, but the government is increasingly focusing on the use of generics and greater openness [Source: IQVIA Market Prognosis, October 2017].

Australia

Australia's pharmaceutical market is set to grow marginally from US$ 13 Billion in 2017 to US$ 16 Billion by 2022, registering 1-4% CAGR [Source: IQVIA Market Prognosis, October 2017].

The Australian government is playing a proactive role in ensuring a wider adoption of generics in clinical practice and lowering the prices of medicines in the country. A recent study by Grattan Institute concluded that the prices of crucial branded drugs in Australia were higher in comparison to its developed counterparts across the world. The government announced a series of interventions to encourage physicians to prescribe generic products, with the objective of bringing generic use to 80% vis-à-vis branded drugs.

Currently, Australia's medicine sales are driven by rising demand for treatments, successful innovation, product line expansion, strong clinical study outcomes and various FDA approvals. The revamped drug approval process and the proposed upgradation of outdated cost-push regulations will also benefit the industry.

Pharmerging markets

The pharmaceutical spending in pharmerging markets stood at around US$ 269.6 Billion in 2017. It is estimated to grow at 6-9% CAGR during the next five years, to reach US$ 345-375 Billion in 2022 [Source: IQVIA Market Prognosis, October 2017].

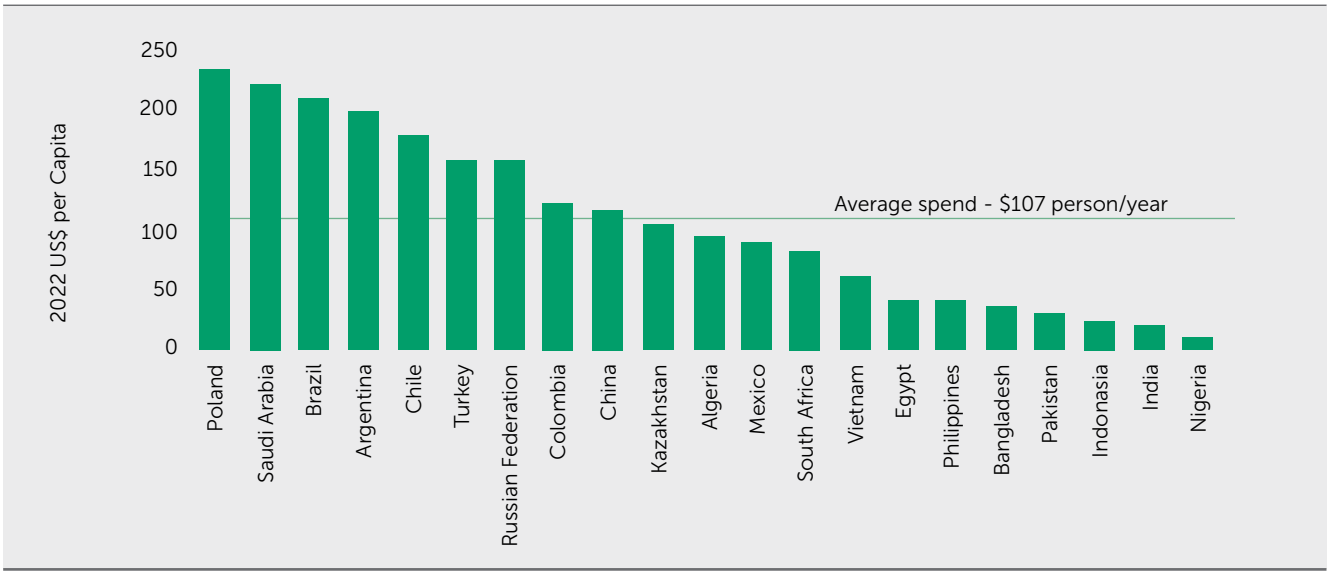
Pharmaceutical spending in pharmerging markets

(US$ Billion)

Region/Country	2017	2013-2017 CAGR	2022	2018-2022 CAGR
Pharmerging markets	269.6	9.7%	345-375	6-9%
China	122.6	9.4%	145-175	5-8%
Tier 2	67.3	11.2%	89-93	7-10%
Brazil	33.1	11.5%	38-42	5-8%
India	19.3	11%	26-30	9-12%
Russia	14.9	10.8%	20-24	7-10%
Tier 3	79.7	8.9%	95-125	6-9%

[Source: IQVIA Market Prognosis, October 2017]

Pharmerging countries' medicines spend per capita in 2022



Source: IQVIA Market Prognosis, September 2017; IQVIA Institute October 2017
Notes: Spending per capita, per capita growth and overall spending growth in Constant US$

China

China, the world's largest pharmerging market, is likely to grow by a CAGR of 5-8% over the next five years to reach US$ 145-175 Billion in 2022 [Source: IQVIA Market Prognosis, October 2017]. The new Generic Quality and Efficacy Evaluation guidelines in China are intended to drive registration and development of bioequivalent generics. Off-patent originators, at present, account for nearly 18% of spending in China [Source: IQVIA 2018 and Beyond, March 2018]. Estimates suggest that 50-85% of this spending on off-patent originators could shift to bio-equivalent, locally produced generics within the next half-decade [Source: IQVIA 2018 and Beyond, March 2018].

Africa

Africa's pharmaceutical industry is expected to grow from US$ 20.8 Billion in 2013 to reach US$ 40-65 Billion by 2020 [Source: McKinsey & Company]. This growth is driven by an expansion of primary health care capacity. The continent is likely to be responsible for a significant proportion of pharmerging markets' spending in the coming decades and portends well for multi-national pharmaceutical companies seeking new growth avenues.

The major problem for Africa is the establishment of a reliable supply and distribution mechanism, due to underdeveloped regulations and insufficient logistical infrastructure. Healthcare challenges in some African countries translate into future opportunities for industry players. South Africa continues to be the largest market in pharmaceuticals among other African nations.

About Strides

Incorporated in 1990, Strides is a global pharmaceutical company that operates across two business verticals in regulated markets and emerging markets. We have a strong commercial presence across 100+ countries and are headquartered in Bangalore.

We have a global manufacturing footprint with eight production units spread across three continents. Six of our manufacturing facilities cater to regulated markets and have key regulatory approvals including USFDA, UK MHRA, TGA, PMDA ANVISA, WHO. We also own two dedicated production facilities for the emerging markets.

We enjoy robust research and development (R&D) infrastructure in India with global filing capabilities. Our R&D capabilities help us to develop and manufacture a wide range of niche and technically complex pharmaceutical products. We are also among the world's largest soft gelatin capsule manufacturers.

Evolution of Strides 2.0

At Strides, our objective is to build a diversified consumer-focussed global formulations business. We have evolved as a global B2C pharmaceutical company and our primary focus today is on further developing our front-end presence in regulated and emerging markets to achieve considerable scale. Over the last few years, we have put together the building blocks to commence the next leg of our journey. In the last three years, we have made significant investments in strategic acquisitions, capacity expansions, R&D, IT infrastructure and compliance to build a strong foundation for Strides 2.0. Our strategic initiatives have helped us attain critical size and has repositioned the Company as a well-diversified, consumer-facing formulations player with an enhanced focus towards regulated markets.

We have robust front-end presence in the regulated markets of Australia, the US and the UK. We also have presence in continental Europe through strategic partnerships. We have six facilities for regulated markets (five with USFDA approval) in India, Singapore and Italy that complement our business. We have an R&D centre in Bangalore which is focussed on developing and filing niche and differentiated products for global markets. Our emerging markets business comprises our front end presence in sub-saharan Africa region through our branded business and we also work closely with donor funding agencies for supplies of anti retrovirals and anti malarial products.

Regulated markets

USA

Amidst macro headwinds, US still the largest growth market with a recalibrated strategy

In the US market, we operate the front-end business through our subsidiary, Strides Pharma Inc. We are on the cusp of getting to a critical size in the US. Our focus is mainly on niche, low volume, low competition, high technology barrier products built around modified releases (MRs), soft-gel capsules (SGCs), topicals and liquids. We also produce high competition products where we enjoy the benefits of a fully integrated value chain through our most preferred customer status with Solara Active Pharma Sciences for the API supplies.

At the end of FY 2017-18, we had a portfolio of 74 filed ANDAs (with 30 pending approvals). Several of our commercialised products in the US are ranked amongst top 3 on a volume market share. We also have received several customer award including the Cardinal Health Supply Chain Excellence Award for 2017.

Going forward, we will utilise our R&D capabilities for 20-25 filings every year to benefit from new Generic Drug User Fee Act (GDUFA) regulations. Additionally, we will reduce dependence on partnership business and in the coming years, we will leverage our front-end presence to scale our business.

Key highlights of FY 2017-18

- Sustained R&D investments at ₹1,176 Million against ₹1,070 Million in the previous year
- Product filing and approval gained momentum with 12 new ANDA filings and 14 product approvals received
- Continued to gain market share for front-end products: Ranitidine (35%), Dutasteride (33%), Ergocalciferol (38%), Methoxsalen (40%), Benzonatate (16%) and PEG Rx (25%)
- Witnessed single-digit price erosion for front-end portfolio

Outlook

- Recalibrate strategy with a front-end bias towards sustainable growth
- Exiting partnership business with no new partnership contracts being signed. Around 50% of value under partnership business to be launched through our front-end by end of FY 2018-19
- Ensure filings momentum with 20-25 ANDA filings per year
- Expand own front end to deliver growth
- Intend to launch 15 new products in FY 2018-19

Australia

Bolster our Australian leadership positioning with margin improvements

After re-entering Australia through the acquisition of Arrow in 2015 and several business initiatives, we are now ranked No. 2 by volumes and No. 3 in revenues in the Australian generics market.

We have a long-term relationships with Sigma (largest wholesaler in Australia) and Pharmacy Alliance (a group company) that have helped improve our pharmacy footprint. Going forward, we expect a double-digit growth rate ahead of the market. We are focused on increasing our pharmacy footprint and expanding our product portfolio through in-house development and by in-licencing products.

With our intent to merge our Australian business with Apotex, we expect to be a market leader in Australia's generics pharmaceutical industry (subject to certain customary closing conditions and statutory approvals).

Key highlights of FY 2017-18

- Achieved ramp-up with increase in pharmacy footprint to 1,400+ and launch of 29 new products
- Expanded margin by leveraging efficient operations and supply chain, including site transfer to in-house manufacturing
- Recorded robust performance in Chemist's Own OTC portfolio
- Completed integration of the Amneal acquisition

Outlook

- Expect to grow ahead of markets with sustained margins
- Expand product portfolio in Rx and OTC segments
- Further enhance pharmacy footprint
- Improve throughput with better compliance for Arrow products at store level
- Leverage our in-house manufacturing base in India and Singapore to deliver further cost of goods sold (COG) savings

Other regulated markets

Leveraging strong regulated market portfolio through portfolio maximisation

Other regulated markets for us comprises all regulated markets excluding the US and Australia. As part of our portfolio maximisation strategy, we are enhancing our presence across other regulated markets, which provide significant opportunities. We are focussed on leveraging our wide-ranging regulated market portfolio to build a low investment high return opportunity in these markets.

Key highlights of FY 2017-18

- Continued traction in the UK front-end
- Introduced new products and improved market share for key molecules in rest of Europe aided growth in the region
- Forayed recently into high entry-barrier market of South Africa through acquisition of controlling stake in Trinity Pharma

Outlook

- Expand UK front end through more Rx and OTC listing at wholesalers
- Multiply product offering through strategic collaborations in the rest of Europe, including entry into new geographies
- Capitalise on Trinity's established distribution channel in South Africa for faster commercialisation of existing Strides products including ARV portfolio in non-tender market

Emerging markets

Institutionalise efficiencies for a profitable African and emerging market branded generics play

Our focus is on creating a leading branded generics platform in Africa by leveraging our portfolio of mega brands.

Africa

In Africa, we are pursuing the 'In Africa, for Africa' strategy. At present, we have significant sales footprint with presence in over 40+ Sub Saharan African countries and we also have access to one of the very few WHO approved sites in the region. We have a robust medical field force in Africa that has helped us extend our reach to over 30,000 doctors. We currently have 750 products registered and a pipeline of 500+ product registrations. We also enjoy strong brand equity with doctors and the community at the local level. In Africa, our objective is to attain a leadership position in key markets with a focus on lifestyle chronic therapies driven by brands.

Key highlights of FY 2017-18

- Delivered healthy secondary sales growth of 22% for branded business in French Africa (according to IMS) and recorded 2x of market growth
- Focussed on maintaining a healthy primary to secondary sales ratio

- Key brands including - Renerve, Solcer, Combiart continue to maintain healthy market share

Outlook

- Focus on building a portfolio of power brands
- Maintain market leading secondary sales growth trend for brands business in Africa
- Continued focus on better balance of primary and secondary sales
- Drive margin expansion through superior product portfolio and improved MR productivity
- Expand footprint in East Africa to strengthen the branded generic platform in Africa

Institutional business

Focus on new treatment regimens

We develop and manufacture drugs in the anti-retroviral and anti-malarial segments for our institutional business. Our customers for this business segment include institutionally-funded aid projects and global procurement agencies. We have filed dossiers with product registrations across emerging markets. We continue to strengthen our R&D initiatives to develop next-generation products according to donor agency guidelines to enhance our growth in this segment. Moreover, we will leverage our strong visibility with innovator organisations to be among the first wave of launches in select emerging markets.

Key highlights of FY 2017-18

- Reported a challenging year for ARV business with compressed margin for supplies under long-term contracts
- Witnessed non-viability of certain businesses at current pricing levels due to the disruption of the API supply chain globally
- Retained our market share in the new malaria tender, however, the overall tender size has shrunk by ~50% top line

Outlook

- Forecast of subdued growth in a challenging business environment
- Expect weakness in Antimalaria to continue in current year
- Improve business margins by renegotiating pricing for ARV contracts
- Introduced next generation ARV drugs in line with evolving treatment regimens - products already in R&D pipeline for development
- Stay invested in institutional business as it helps recover manufacturing cost

Financial Highlights

Consolidated

₹ in Million

Particulars	FY 2016-17	FY 2017-18
Revenues	27,581	28,576
EBIDTA	6,027	4,369
EBIDTA margin (%)	22	15

People at our core

We are as good as our teams that drive our growth trajectory. Our focus remains steady on attracting and retaining the best industry talent, nurturing them in a friendly workplace and motivating them to shoulder challenging responsibilities.

We foster merit-based recruitments and support adequate training to enhance skill-sets and upgrade their knowledge. We also impart leadership and managerial development training for improved performance of our team. These interventions help motivate our people to ensure organisational excellence. Besides, with curriculum-based learning programmes, we help our people to improve efficiency consistently. We have employee-friendly HR policies to boost the motivation levels of our teams and keep them aligned with the Company's vision. Moreover, we have built a multi-cultural and diverse workforce which comprised 2,100+ members as of March 31, 2018.

Round-the-clock risk governance

Risks	Risk definition	Risk mitigation
Regulatory risk	We operate in a highly regulated industry. Any failure to comply with applicable regulations may adversely impact our operations and business growth.	• Consistent track record of approvals from all leading global regulatory authorities • Regular inspection of production facilities for compliance with current Good Manufacturing Practices (cGMP); and such compliance is assessed by the World Health Organisation (WHO) and USFDA • Routine upgradation of audit procedures to comply with any changes in international regulatory requirements, such as those of US FDA, MHRA (United Kingdom), ANVISA (Brazil) and TGA (Australia), among others
Research and development risk	If we are incapable of pushing the innovation envelope, we may fail to capitalise on emerging opportunities.	• Our dedicated R&D efforts are directed towards innovative technologies, designed to expand our product portfolio. • Our R&D facility is located in India — Bengaluru • Filed application for 12 ANDAs in the US
Operation risk	Our profitability and margins can decline in case our raw material supply gets interrupted or operational cost rise.	• Long-term contracts with approved vendors (domestic and global) after stringent vendor audit ensures supply of raw materials • Round-the-clock review mechanism to enhance optimum utilisation of operational facilities • Our globally benchmarked manufacturing facilities are certified by the world's top regulatory authorities for production efficiency
Quality risk	Our business may be adversely impacted if there are manufacturing or quality control challenges. This may further expose us to litigation or other liabilities, which may adversely affect our business.	• We continue to elevate our quality assurance procedures in line with global standards • Our quality control department ensures materials are received from our approved lists of vendors; and materials comply with internal standards and specifications
Marketing risk	We may not be able to evolve the relevant marketing approach for faster customer outreach, which may jeopardise product offtake and hamper growth.	• Presence in 100+ countries • **USA:** Front-end presence selling products to key wholesalers • **UK:** Primarily supply generics to hospitals approved by the NHS; and OTC products through retail outlets • **Europe:** Out-licensing agreements with key players for sales in the continent • **Australia:** Partnering with Sigma and Pharmacy Alliance allows us access to around 1,400 pharmacies. Proposed merger will Apotex will make us one of the leading pharmaceutical company in Australia • **Africa:** Significant field team drives our branded generics business • Approved supplier with global organisations, such as UNITAID, PEPFAR and CHAI to supply anti-retroviral and anti-malarial drugs to institutionally funded aid projects and global procurement agencies
Information technology risk	IT-enabled systems and processes enhance integration and accelerate decision-making. Our inability to implement advanced technologies or lack of a strong IT framework and infrastructure may impact business operations	• Secured IT network, achieved by implementing firewall, intrusion prevention system (IPS), network segregation and end-point security solutions • Routine validation check of business processes under the Good Manufacturing Practices (GMP)

Internal control systems and adequacy

The Company's advanced IT infrastructure ensures adequate internal controls over business processes and practices. This internal control system provides reasonable assurance about the integrity and reliability of financial statements. Moreover, the Company has a strong in-system audit programme, supported by Grant Thornton, which regularly encompasses various operations consistently. Our Audit Committee reviews internal audit observations regularly.